Supreme Court, U.S.
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No. 98-1291

In the
Supreme Court of the United States
October Term, 1998

CONNECTICUT VALLEY ELECTRIC COMPANY and CENTRAL VERMONT PUBLIC SERVICE CORPORATION

Petitioners,

v.

DOUGLAS L. PATCH, BRUCE B. ELLSWORTH, and SUSAN S. GEIGER,

Respondents.

BRIEF OF RESPONDENTS DOUGLAS L. PATCH, ET AL. IN OPPOSITION TO THE PETITION

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QUESTION PRESENTED

Whether a state public utility commission has jurisdiction to find a retail electric utility imprudent for not exercising its right to terminate a wholesale power purchase contract and purchase cheaper alternative power, under a termination provision contained in the wholesale power contract on file with and approved by the Federal Energy Regulatory Commission.

TABLE OF CONTENTS

QUESTION PRESENTED.....i

TABLE OF CONTENTS..... ii

TABLE OF AUTHORITIES.....iii

STATEMENT OF THE CASE..... 1

REASONS FOR DENYING THE WRIT..... 3

The NHPUC's Finding Of Imprudence Is Not Preempted Under The Federal Power Act..... 4

1. Congress intended a harmonious, dual system of regulation..... 4
2. The filed-rate doctrine does not preempt the NHPUC from finding CVEC imprudent..... 6
3. The NHPUC's exercise of jurisdiction over CVEC's decision not to terminate its purchases comports with every case reviewing the issue..... 9
4. FERC recognizes state authority over purchase decisions.....12

CONCLUSION.....13

TABLE OF AUTHORITIES

Cases

Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375 (1983) 4
Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) 5
Gulf States Utilities Co. v. Public Util. Comm'n, 841 S.W.2d 459 (Tex. Ct. App. 1992) 10
Kentucky West Virginia Gas Co. v. Pennsylvania Pub. Util. Comm'n, 837 F.2d 600 (3rd Cir.), *cert. denied*, 488 U.S. 941 (1988) 3, 9
Louisiana Pub. Serv. Comm'n v. Federal Communications Comm'n, 476 U.S. 355 (1986) 4
Mississippi Power & Light Co. v. Moore, 487 U.S. 354 (1988) 3, 7, 8, 13
Nantahala Power and Light Co. v. Thornburg, 476 U.S. 953 (1986) ..... *passim*
Narragansett Elec. Co. v. Burke, 381 A.2d 1358 (R.I. 1977), *cert. denied*, 435 U.S. 972 (1987) 6
New Orleans Pub. Serv., Inc. v. Council of New Orleans, 911 F.2d 993 (5th Cir. 1990), *cert. granted*, 499 U.S. 974, *cert. dismissed*, 502 U.S. 954 (1991) 9
Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n, 332 U.S. 507 (1947) 6
Pike County Light and Power Co. v. Pennsylvania Pub. Util. Comm'n, 465 A.2d 735 (Pa. Commw. Ct. 1983) 7, 11, 12
Public Utilities Comm'n v. United Fuel Gas Co., 317 U.S. 456 (1943) 5
Public Utilities Comm'n v. Attelboro Steam & Electric Co., 273 U.S. 83 (1927) 5
Rice v. Santa Fe Elevator Corp., 331 U.S. 218 (1947) 4
Sinclair Machine Products, Inc., 498 A.2d 696 (1985) 11
United States v. Public Utilities Comm'n, 345 U.S 295 (1953) 6

TABLE OF AUTHORITIES -- Continued

Cases - Continued

Wisconsin Pub. Intervenor v. Mortier,
501 U.S. 597 (1991) 4

Statutes

15 U.S.C. § 717 5
16 U.S.C. § 824 5

Agency Orders

Federal Energy Regulatory Commission

Central Vermont Pub. Serv. Corp., 81 F.E.R.C.
(CCH) ¶ 61,336 (1997), *rehearing denied*,
84 F.E.R.C. (CCH) ¶ 61,295 (1998) 8
Central Vermont Pub. Serv. Corp., 84 F.E.R.C.
(CCH) ¶ 61,194 (1998) 9, 12
Doswell Ltd. Partnership, 50 F.E.R.C. (CCH)
¶ 61,251 (1990) 12
Pennsylvania Power and Light Co., 23 F.E.R.C.
(CCH) ¶ 61,325 (1983) 13
Philadelphia Elec. Co., 15 F.E.R.C. (CCH)
¶ 61,264 (1981) 13
Transcontinental Gas Pipe Line Corp.,
57 F.E.R.C. (CCH) ¶ 61,344 (1991) 13

New Hampshire Public Utilities Commission

Connecticut Valley Elec. Co., 71 NHPUC 145 (1986) 2
Re Concord Elec. Co., 69 NHPUC 701 (1984) 2

STATEMENT OF THE CASE

Except for limited purchases mandated by statute, Connecticut Valley Electric Company ("CVEC"), a small retail electric distribution company in New Hampshire, purchases all of the power needed to serve its approximately 10,000 retail customers from its parent, Central Vermont Public Service Corporation ("CVPS"). These purchases are made under a wholesale contract, denominated the RS-2 Rate Schedule, filed with and approved by the Federal Energy Regulatory Commission ("FERC"). CVEC has purchased power from CVPS under the RS-2 Rate Schedule since 1983. In addition to provisions regarding the pricing and other terms of the delivery of electricity, the RS-2 Rate Schedule provides, under Section E, entitled "Termination:"

> Service under this Rate Schedule may be terminated at any time if both the Company and the Customer agree to the termination. If there is no agreement, service may be terminated at the end of a service year if the party seeking termination has given written notice of termination prior to the beginning of that service year.

Pet. App. 131.

The respondents are the Chairman and Commissioners of the New Hampshire Public Utilities Commission ("NHPUC"). Pursuant to its authority under New Hampshire law, the NHPUC first reviewed CVEC's participation in the RS-2 Rate Schedule in 1986. In its order initially approving CVEC's purchases under the RS-2 Rate Schedule, the NHPUC concluded:

> After review and consideration, we find that CVEC has met its burden of proving that its

> participation in the RS-2 rate with CVPS is reasonable....
>
> Our findings and conclusions in this proceeding will not necessarily be the same in future dockets. The terms of the RS-2 tariff provide that CVEC may terminate the arrangement on one calendar year's notice.[n4]
>
> ---
>
> [n4]The Commission has previously provided that it favors power supply arrangements which will allow the Commission to review periodically the decisions of the regulated distribution company. *Re Concord Electric Company*, 69 NHPUC 701, 705, 706 (1984). The one year termination provision in the CVPS RS-2 rate satisfies the Commission's concern in this area.

Connecticut Valley Elec. Co., 71 NHPUC 145, 147 (1986).

In late 1997, the City of Claremont, New Hampshire, where the majority of CVEC's retail customers reside, filed a complaint with the NHPUC alleging that CVEC's continued purchase from CVPS was imprudent. Shortly thereafter, CVEC submitted its annual purchased power cost adjustment and fuel adjustment clause filing with the NHPUC, seeking an increase in retail rates due to an increase in purchased power and fuel costs. At a duly noticed hearing of both matters, the NHPUC considered evidence showing that CVEC could purchase power from entities other than its parent at substantially lower costs than those charged under the RS-2 Rate Schedule. The NHPUC entered an order freezing CVEC's retail rates at their December 31, 1997 level

based on its initial finding that CVEC was imprudent for not terminating the purchases under the RS-2 Rate Schedule. Pet. App. 114-116. The District Court entered an injunction requiring that the NHPUC allow CVEC's proposed higher rates to go into effect. Pet. App. 79. The First Circuit vacated that injunction in its opinion dated December 3, 1998. Pet. App. 1.

REASONS FOR DENYING THE WRIT

The NHPUC, in the exercise of its statutorily mandated authority, ruled that CVEC was imprudent because it elected to continue purchasing power from its parent despite (1) CVEC's contractual ability to terminate those purchases and (2) the availability of cheaper alternative power supplies. Nothing about that ruling warrants United States Supreme Court review. The decision of the First Circuit Court of Appeals upholding the NHPUC's authority is based on the clear and unambiguous language contained in the contract on file with and approved by FERC, is in accord with a decision of the Third Circuit Court of Appeals in a similar context, *Kentucky West Virginia Gas Co. v. Pennsylvania Pub. Util. Comm'n*, 837 F.2d 600 (3rd Cir.), *cert. denied*, 488 U.S. 941 (1988), and is within the exception to the filed-rate doctrine recognized by this Court in *Nantahala Power and Light Co. v. Thornburg*, 476 U.S. 953, 972 (1986) (observing that "a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*."). *Accord Mississippi Power & Light Co. v. Moore*, 487 U.S. 354 (1988). Because the First Circuit decision does not create a conflict in the circuit courts, does not raise any issue of national importance, does not contravene FERC's own understanding of its jurisdiction, and does not conflict with the rulings of this Court

concerning the limits of federal jurisdiction, the writ should be denied.

The NHPUC's Finding Of Imprudence Is Not Preempted Under The Federal Power Act.

1. Congress intended a harmonious, dual system of regulation.

Where a federal statute is applicable, the scope of the preemptive power of that law depends on congressional intent. *See Wisconsin Pub. Intervenor v. Mortier*, 501 U.S. 597, 604 (1991). As the Court explained in *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 229-30 (1947) (citations omitted): "Congress may, if it chooses, take unto itself all regulatory authority, . . . share the task with the States, or adopt as federal policy the state scheme of regulation. The question in each case is what the purpose of Congress was." When considering questions of preemption, the analysis must "start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." *Wisconsin Pub. Intervenor*, 501 U.S. at 605 (quoting *Rice*, 331 U.S. at 230).

The instant case involves the regulation of electric utilities, which this Court has recognized to be "one of the most important of the functions traditionally associated with the police powers of the States." *Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983). Given its importance under the police power of the States, traditional state regulation of utilities cannot be preempted unless there is a "clear and manifest" intent to do so in the federal statutory scheme. *See Louisiana Pub. Serv. Comm'n v. Federal Communications Comm'n*, 476 U.S. 355, 369 (1986).

The Federal Power Act, 16 U.S.C. § 824 *et seq.* ("FPA"), shows no "clear and manifest" intent to supersede the traditional state regulation of utilities. To the contrary,

> It is clear, as the legislative history of the Act amply demonstrates, that Congress meant to create a comprehensive scheme of regulation which would be complementary in its operation to that of the states, without any confusion of functions. The Federal Power Commission would exercise jurisdiction over matters in interstate and foreign commerce to the extent defined in the Act, and local matters would be left to the state regulatory bodies. Congress contemplated a harmonious, dual system of regulation of the natural gas industry – federal and state regulatory bodies operating side by side, each active in its own sphere.

Public Utilities Comm'n v. United Fuel Gas Co., 317 U.S. 456, 467 (1943) (citation omitted).[1]

A dual system of regulation was needed to "fill the gap" in regulation over interstate sales and transmission of electricity found to exist by *Public Utilities Commission v. Attelboro Steam & Electric Co.*, 273 U.S. 83 (1927). The FPA was expressly designed to assert federal regulation over this gap: "Congress interpreted [*Attleboro*] as prohibiting state control of wholesale rates in interstate commerce for resale, and so armed the Federal Power Commission with

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[1] Although this case interpreted the jurisdictional provisions of the Natural Gas Act, 15 U.S.C. § 717 *et seq.*, the provisions of that Act are virtually identical to those in the Federal Power Act regarding the scope of federal jurisdiction, and cases interpreting equivalent sections of the two acts may be cited interchangeably. *See Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981).

precisely that power." *United States v. Public Utilities Comm'n*, 345 U.S 295, 307-308 (1953). This interpretation guided the delineation of federal and state jurisdiction under the FPA:

> The line of the statute was thus clear and complete. It cut sharply and cleanly between sales for resale and direct sales for consumptive uses. No exceptions were made in either category for particular uses, quantities or otherwise. And the line drawn was that one at which the decisions had arrived in distributing regulatory power before the Act was passed.

Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n, 332 U.S. 507, 517 (1947). Thus, state utility commissions retain jurisdiction over all matters relating to the regulation of electric energy unless Congress has specifically conferred jurisdiction on FERC.

2. The filed-rate doctrine does not preempt the NHPUC from finding CVEC imprudent.

One preemption doctrine that has emerged is the so-called "filed-rate doctrine." Under this doctrine, a state may not substitute its judgment about cost elements reviewed by FERC in approving a wholesale tariff to prevent a wholesale purchaser from recovering at retail the costs of paying a FERC-approved wholesale rate. *See, e.g., Narragansett Elec. Co. v. Burke*, 381 A.2d 1358, 1362 (R.I. 1977), *cert. denied*, 435 U.S. 972 (1978).

Subsequent decisions under the filed-rate doctrine demonstrate that federal preemption of state utility commissions can occur in three ways, none of which is implicated by the actions of the NHPUC in this case. First,

once FERC sets a wholesale rate as just and reasonable, no court may alter that particular rate on the ground that, in its opinion, a different rate is more reasonable. *Nantahala*, 476 U.S. at 966. Second, in setting just and reasonable wholesale rates, FERC's determination encompasses both the rates themselves and the FERC-mandated power allocations or cost allocations that affect wholesale rates. *Id.*; *Mississippi Power*, 487 U.S. at 371. Finally, once FERC approves the wholesale rates, a state utility commission may not prevent a regulated utility from passing through those rates to retail customers. *Nantahala*, 476 U.S. at 970; *Mississippi Power*, 487 U.S. at 372.

A well recognized exception to the filed-rate doctrine has also developed. That exception, first recognized in *Pike County Light and Power Co. v. Pennsylvania Public Utility Commission*, 465 A.2d 735, 738 (Pa. Commw. Ct. 1983) holds that while a state cannot review the reasonableness of the wholesale rate set by FERC, the state may determine whether it is in the public interest for a purchaser under its jurisdiction to purchase that power in light of its available alternatives. This Court has recognized the exception to the filed-rate doctrine in both *Mississippi Power*, 487 U.S. at 373-74, and *Nantahala*, 476 U.S. at 972, where this Court assumed, without deciding, that "it might well be unreasonable for a utility to purchase unnecessary quantities of high-cost power, even at FERC-approved rates, if it had the legal right to refuse to buy that power." In this matter, CVEC has the legal right under the FERC-approved RS-2 Rate Schedule to terminate further purchases from its parent. *See* Pet. App. 131.

The NHPUC's determination that CVEC was imprudent for failing to exercise its termination rights is not preempted by FERC's approval of the underlying rate schedule. CVEC, a retail distribution company, is not subject to the jurisdiction of FERC, and FERC has not and could not

determine the prudence of CVEC's purchases from CVPS. Further, the NHPUC's action has not disturbed or challenged the rate charged by CVPS under the RS-2 Rate Schedule. CVPS is free to charge the RS-2 rate to whomever is willing to pay it. The NHPUC simply found that, given available lower-priced alternatives, CVEC was imprudent for not exercising its right pursuant to the contract to terminate, and instead continuing to purchase from CVPS.

Despite the petitioners' arguments to the contrary, Petition at 16-19, there is no FERC-mandated allocation of costs affecting the wholesale rates in the RS-2 Rate Schedule. The RS-2 Rate Schedule contains formulae which are used to compute unit rates to recover CVPS's systemwide costs. The principal rates are the energy rate and the capacity rate. The energy rate is computed by dividing CVPS's energy costs by total kilowatt hours of energy produced or purchased for sale to all CVPS customers, including CVEC. The formula does not produce a separate CVEC unit rate, but a total CVPS system unit rate. The capacity rate is a monthly rate and is computed as one-twelfth of the product of CVPS's annual generation and transmission capacity cost and CVEC's proportional usage of those facilities. Fundamentally, both the capacity and energy rate charged to CVEC are based on usage, and, thus, the RS-2 Rate Schedule cannot be said to contain an interstate allocation agreement. Pet. App. 132-135, 142-150. Most importantly, on two separate occasions, FERC has ruled that the RS-2 Rate Schedule is not an allocation agreement. *Central Vermont Pub. Serv. Corp.*, 81 F.E.R.C. (CCH) ¶ 61,336 at 62,542-3 (1997), *rehearing denied*, 84 F.E.R.C. (CCH) ¶ 61,295 at 62,371 (1998). Specifically, FERC found:

> This case does not present the same fact situation as *Mississippi Power* or *Nantahala*. The Commission, through its approval of the wholesale rate schedule between Central

> Vermont and Connecticut Valley, did not dictate a specific cost or power allocation of the type at issue in *Mississippi Power* or *Nantahala*. Additionally, in approving the rates, terms and conditions of the RS-2 rate schedule, the Commission did not make any determination that it was prudent for the purchaser to enter into the contract in the first place, or whether, over time, it has become imprudent for the purchaser not to exercise its termination rights under the contract in order to purchase cheaper power elsewhere.

Central Vermont Pub. Serv. Corp., 84 F.E.R.C. (CCH) ¶ 61,194 at 61,975 (1998). Therefore, because the NHPUC's actions do not disturb the wholesale RS-2 rate and the RS-2 Rate Schedule does not contain a FERC-mandated allocation of costs, no action of the NHPUC is precluded under the filed-rate doctrine.[2]

3. The NHPUC's exercise of jurisdiction over CVEC's decision not to terminate its purchases comports with every case reviewing the issue.

In 1988, the Third Circuit had occasion to review a state commission's decision finding a utility's continued gas purchases from an affiliate at FERC-approved rates imprudent given the availability of cheaper alternatives. *Kentucky West Virginia Gas Co. v. Pennsylvania Pub. Util. Comm'n*, 837 F.2d 600 (3rd Cir.), *cert. denied*, 488 U.S. 941

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[2] Nor does this case involve a situation similar to *New Orleans Public Service, Inc. v. Council of New Orleans*, 911 F.2d 993 (5th Cir. 1990), *cert. granted*, 499 U.S. 974, *cert. dismissed*, 502 U.S. 954 (1991). In that case, there was an allegation that action of the Council of New Orleans affected a FERC-mandated cost allocation concerning Grand Gulf nuclear costs. Here, there is no cost allocation approved or mandated by FERC and thus the issues are distinct.

(1988). The Third Circuit confirmed the authority of the Pennsylvania Public Utility Commission to find that the distributor acted imprudently in continuing to purchase from its affiliate despite the fact that the gas being purchased was sold at a FERC-approved price. In upholding the Pennsylvania Commission's authority, the Court stated:

> Although *Nantahala* underscores that a state cannot independently pass upon the reasonableness of a wholesale rate on file with FERC, it in no way undermines the long-standing notion that a state commission may legitimately inquire into whether the retailer prudently chose to pay the FERC-approved wholesale rate of one source, as opposed to the lower rate of another source.

Id. at 609. Thus, the Third Circuit and First Circuit are in accord on the issue.

All other courts considering the issue have recognized the ability of the appropriate state regulatory body to review purchase decisions in evaluating the reasonableness of retail rate tariffs. No court has found that federal authority precludes such review:

> Section 824 of the FPA expressly grants FERC jurisdiction to regulate *sales* of wholesale power in interstate commerce; FERC's inquiry focuses on the rates at which *sellers* market their power. FERC does not review the market conditions or other factors that govern the prudence of the purchaser's decision to buy power in the wholesale transaction.

Gulf States Utilities Co. v. Public Util. Comm'n, 841 S.W.2d 459, 465 (Tex. Ct. App. 1992). That Court went on, after

conducting a thorough review of the prior case law, including FERC precedent, to indicate that where "a utility has a choice to purchase a particular quantity of power at a particular price, the state may properly review the utility's prudence in incurring that expense." *Id.* at 469.

In the instant matter, FERC's review of the RS-2 Rate Schedule focused on the reasonableness of CVPS's wholesale rate, which was not at issue before the NHPUC. In contrast, the NHPUC addressed CVEC's purchase decision in light of the alternatives and its ability to terminate the contract with CVPS. The NHPUC may properly address this issue under the authority reserved to the states:

> The FERC focuses on [the wholesaler] to determine whether it is just and reasonable *for that company to charge* a particular rate, but makes no determination of whether it is just and reasonable *for [the retailer] to incur* such a rate as an expense. The PUC, on the other hand, has no jurisdiction to analyze [the wholesaler's] cost of service and makes no determination as to the reasonableness for [the wholesaler] to charge its rates. The PUC focuses on [the retailer] and its cost of service data to determine whether it is reasonable for [the retailer] to incur such costs in light of available alternatives.

Pike County, 465 A.2d at 738.

The Supreme Court of New Hampshire also recognized the guiding principle in *Sinclair Machine Products, Inc.*, 498 A.2d 696, 699 (1985):

> The PUC correctly determined under federal preemption principles that FERC approval of wholesale rate precludes the PUC from

> questioning the *reasonableness of that charge.* However, it does not follow *automatically* that the PUC must find that power costs incurred under a wholesale rate are *necessarily a reasonable expense for the retailer.*

Because CVEC could exercise its termination rights and purchase cheaper power elsewhere, it had a choice of power suppliers. CVEC's failure to avail itself of those alternatives is properly subject to a prudence review by the NHPUC.

4. FERC recognizes state authority over purchase decisions.

The NHPUC's exercise of jurisdiction over CVEC's purchase decisions is consistent with FERC's understanding of the jurisdictional boundaries of federal and state authority. FERC has repeatedly indicated that States are free to evaluate the reasonableness of a retail utility's (here, CVEC) purchase decisions, despite a FERC finding of reasonableness regarding the rates charged by the wholesaler (here, CVPS) supplying the utility. In the context of the present controversy, FERC has ruled:

> The Commission's decisions and its long-standing practice in setting wholesale rates support the *Pike County* exception to the *Narragansett* doctrine. . . . [A] state commission is not precluded under the FPA from reviewing the prudence of a wholesale purchase that was made at Commission-approved rates if the purchaser had other legal choices available.

Central Vermont Pub. Serv. Corp., 84 F.E.R.C. (CCH) ¶ 61,194 at 61,975 (1998). *See also, Doswell Ltd. Partnership*, 50 F.E.R.C. (CCH) ¶ 61,251 at 61,758, n.18 (1990) (stating that FERC "reaffirms its conclusion that the Supreme Court's

decisions in [*Nantahala*] or subsequent cases, do not preclude state regulators from reviewing the prudence of a utility's purchasing decisions."); *Pennsylvania Power and Light Co.*, 23 F.E.R.C. (CCH) ¶ 61,325 at 61,716 (1983) ("We do not view our responsibilities under the Federal Power Act as including a determination that the purchaser has purchased wisely or has made the best deal available."); *Philadelphia Elec. Co.*, 15 F.E.R.C. (CCH) ¶ 61,264 at 61,601 (1981) (stating that "we do not mean by this order to prejudge, for our own purposes or those of the respective state commissions, a determination of the prudence of either party in entering into this transaction."); *Transcontinental Gas Pipe Line Corp.*, 57 F.E.R.C. (CCH) ¶ 61,344 at 62,114 (1991) ("state commissions retain the authority under applicable law to investigate the prudence of [local distribution company] gas purchasing practices.").

FERC's interpretation of its jurisdictional authority is entitled to deference. *See, e.g., Mississippi Power*, 487 U.S. at 380-82 (Scalia, J., concurring) ("it is settled law that the rule of deference applies even to an agency's interpretation of its own statutory authority or jurisdiction.") (citations omitted). FERC has determined that a prudence inquiry regarding power purchases by a retail utility with a choice of suppliers is a matter to be resolved by the appropriate state commission.

CONCLUSION

For the foregoing reasons, the Petition for writ of *certiorari* should be denied.

Respectfully submitted,

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